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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

BEFORE THE

Federal Communications Commission

WASHINGTON, D.C. 20554

In the Matter of	)	
	)	
Price Cap Performance Review for Local Exchange Carriers	)	**CC Docket No. 94-1**
	)	

To: The Commission

REPLY COMMENTS OF THE AMERICAN PETROLEUM INSTITUTE

The American Petroleum Institute ("API"), by its attorneys, hereby submits its Reply Comments in response to the Notice of Proposed Rulemaking adopted in the instant proceeding on January 19, 1994, by the Federal Communications Commission ("Commission"), FCC 94-10 (released on February 6, 1994).

INTRODUCTION

API is a national trade association representing approximately 300 companies involved in all phases of the petroleum and natural gas industries, including exploration, production, refining, marketing, and transportation of petroleum, petroleum products and natural gas. Among its many activities, API acts on behalf of its members as spokesperson before federal and state regulatory agencies. The API Telecommunications Committee is one of the standing committees of the organization's Information Systems Committee. The

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Telecommunications Committee evaluates and develops responses to state and federal proposals affecting telecommunications facilities used in the oil and gas industries.

DISCUSSION

The Commission is Urged to Adopt a More Rigorous Approach in Fine-Tuning Price CAP Regulation.

These Reply Comments address several of the many important issues raised in the Notice and addressed at length in the extensive Comments filed by many parties. By and large, API supports the positions advanced by MCI and AT&T and those of the Ad Hoc Telecommunications Users Group ("Ad Hoc") and the International Communications Association ("ICA"). The views expressed by these parties should guide the Commission in ruling on the various issues raised in the Notice. On the other hand, API largely opposes the arguments advanced by the local exchange carriers (LECs), subject to possible agreement that in certain isolated areas competition is emerging in HiCap access and private line services and that a creative approach to structuring an exception or waiver to price caps may be warranted. The recent setback to the Commission's expanded interconnection policy, as a result of Bell Atlantic Telephone Companies et al. v. FCC, strongly suggests, however, the Commission should implement a revised expanded interconnection policy before beginning to structure limited exceptions or waivers to price caps.

General Issue 1: The Goals of Price Cap Regulation Should be Retained Because the LECs are Dominant Carriers.

The Commission is urged to retain the current goals of price cap regulation. The LECs remain dominant access service providers; price caps remain an improvement over rate-of-return regulation; and the goals of price cap regulation, ensuring "LEC rates are just, reasonable, and nondiscriminatory, and [to promote] a communications system that offers innovative high quality services"1/ remain viable. Further, the related purpose of price caps, to encourage "LECs to make economic decisions such as they would make in a fully competitive environmarket,"2/ maximizes the likelihood that the fundamental "competitive result" objective remains central to the Commission's regulation of the LECs.

The Commission is urged to reject the proposal that price caps' goals be expanded to include ensuring that competition can develop in the access markets.3/ The Commission should keep price cap regulation focused on promoting economically efficient behavior by the LECs, while promoting competition through significant "structural" regulation in other proceedings.

1/ Notice, para. 31.

2/ Ibid.

3/ See Comments of Teleport Communications Group, p.4.

The LECs take a contrary position as to the continued vitality of the current goals of price cap regulation, urging they are now subject to significant competition. The LECs' Comments strike virtually identical cords to support this position. The common points include a listing of all of the systems of the competitive access providers (CAPs), utilities, and cable companies maintaining networks in the LECs' service areas (regardless whether these entities are providing special access or switched access services); a map or maps depicting the areas where these other systems are deployed; and citations to any state regulatory decision allowing entry to the LEC markets.4/

The LEC arguments are not persuasive. There is virtually no mention of the technological advantages that the LECs presently possess, such as the absence of local number portability and the increasing concentration of network intelligence in LEC-controlled databases. In the rare instances where a BOC can show that local exchange service competition is authorized, the extent of CAP market penetration is conveniently ignored.

4/ See, e.g., Comments of Bell South, pp. 75-78, and Attachment, Comments on "Transition Issues."

Local exchange competition is in many respects the essential barometer for switched access competition,5/ and local exchange competition is virtually nonexistent. Thus, it is not surprising that CAPs control less than one percent of total access revenues.6/ Moreover, the LECs have roughly $100 billion in recurring depreciation charges, providing substantial funds for reinvestment.7/ With the exception of isolated pockets of competition in HiCap services, as noted above, it is premature to speculate on how to gauge competition in these services or to alter the goals of price caps. A far more pragmatic approach is suggested by AT&T: rather than speculate or attempt to quantify or measure competition at this point in time, the Commission should adopt "regulatory changes that will meaningfully test whether competition is feasible."8/

5/ An extensive discussion on the interrelatedness of various LEC services and switched access is provided by MFS Communications, Inc. ("MFS"). See Comments on MFS, pp. 38-40.

6/ See The Enduring Local Bottleneck, Monopoly Power and the Local Exchange Carriers, Economics and Technology, Inc. Hartfield Associates, Inc., pp. ii (1994).

7/ Id. at p. iii.

8/ Comments of AT&T, pp. 16-18 (a nine-point plan which includes elimination of state exclusive franchise laws and mandating local number portability).

Baseline Issue 1A: Revisions to the LEC Price Cap Plan Are Not Necessary to Support the Development of the National Information Infrastructure.

A number of parties maintain the LECs do not have adequate financial resources or incentives or both to invest in the development of an advanced telecommunications infrastructure. Predictably, several LECs advanced this position.9/ Another party with a vested interest in supra-enhanced infrastructure also urged "more favorable treatment with respect to 'sharing' [of excess earnings], productivity factors, and depreciation."10/ The LECs advocating increased allowable earnings for infrastructure investment never explained how, if they are being pressed by a multitude of competitors thereby warranting far less strict regulation, they can call upon the FCC to modify the regulations so that LEC customers can be charged more to fund greater infrastructure investment.

Unduly generous incentives to fund services for which the demand is highly suspect is a policy doomed to fail.

9/ See e.g., Comments of Southwestern Bell Telephone Company, pp. 68-70. Interestingly, at least one LEC supporting a loosening of LEC regulatory burdens recognized the incongruity of seeking less rigorous regulation on the one hand and requesting greater earnings for LEC infrastructure spending on the other. See Comments of Ameritech, p. 6 ("the most economically efficient way to deploy the most advanced services to the most customers is to let the competitive process do the job").

10/ Comments of the Computer & Communications Industry Association, p.3.

Such an approach would constitute a form of "command and control" regulation at its worst. More particularly, the Commission would be deciding that LECs, as opposed to MFS, other CAPs, or any other potential competitors, are entitled to such a windfall.11/ This would be an extremely unfortunate approach, as noted by ICA:

> [I]t is highly inappropriate for the LEC price cap plan to be converted into some sort of "supply-side" stimulus to the alleged economic development efforts of the telecommunications infrastructure. Increased competition will provide a more efficient mechanism for transferring advanced telecommunications and information technologies into the national economy.12/

A far better approach is to encourage broader-based network investment, as suggested by MCI, by "adopting policies that

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11/ Such an dramatic philosophic change in Commission policy would undermine Commission policies in numerous areas, such as the goal of achieving cost-based IMTS rates. As the Commission is aware, a major justification for inflated non cost-based accounting rates is that many countries have elected to fund other telecommunications services and government services through excessive IMTS rates. Millions of dollars are lost to the U.S. economy because of this balance of payments deficit. Increased LEC earnings for infrastructure development would implicate U.S. policy on international accounting rates.

12/ Comments of ICA, p. 7. The same sentiment was expressed by another user group. See Comments of Ad Hoc, pp. 11-12 ("The bottom line is that consumers, not the FCC, should define the demand for broadband and other information services and, to the extent feasible, marketplace forces should be allowed to operate. . . [and] thereby defining the parameters of the NII in response to actual demand and marketplace forces rather than government edict or LEC caprice").

(1) require the unbundling of access services; (2) encourage cost-based pricing; and (3) ensure nondiscriminatory access to the LEC networks."13/

The Productivity Factor Needs To Be Increased In Order For Price Caps to Operate Effectively as a Surrogate For Competition.

The Commission is urged to adopt the position advanced by MCI, AT&T and others, that the productivity factor has been understated and requires an upward adjustment to 5.9%14/ API will not interpret further the data and studies submitted in response to a Notice on this issue. However, a recent study on productivity in a variety of industries, including telecommunications, merits note. See Service Factor Productivity, McKinsey Global Institute, Washington, D.C., October 1992, Chapter 2E, Telecommunications (hereinafter "Productivity Study"). This study compares the relative productivity of the telecommunications industries of the United States, the United Kingdom, Germany, Japan and France, respectively.

This study focuses on basic telecommunications services; customer premises equipment, central office equipment and value-added services were excluded. The authors relied on measures of labor and capital productivity to calculate a

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13/ See Comments of MCI, p. 13.

14/ Id., at pp. 18-21; see also, Comments of AT&T, pp. 22-28.

"Total Factor Productivity" measure. Under this aggregate measure, the U.S. telecommunications industry is found to be the most productive.15/ However, the study goes on to explain that productivity in the United States would be much higher if the BOCs were subject to competition, or, impliedly, were subject to regulation that better emulated regulation.16/

In assessing the reasons for the differences in the productivity, the authors note the import of regulation:

> [T]he regulatory and competitive environments in which the telecommunications companies operate [are determinative.] The objectives and incentives that an industry environment places before management cause management behavior that fosters or impedes the development of a more productive and innovative industry.17/

The import of the Productivity Study is that if regulation is not sufficiently replicative of a competitive environment, innovation and productivity will be stifled. Moreover, the low productivity of the BOCs as compared to the interexchange carriers strongly suggests that a higher productivity factor is warranted.

An understated productivity factor will negate the potential benefits that incentive regulation can provide. For this reason, a more aggressive productivity factor, as opposed

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15/ Productivity Study, page 17.

16/ Id. at p. 15.

17/ Productivity Study, p.8.

to a reduction as sought by several LECs18/ or retention of the current productivity factor level, would better serve the public interest.

WHEREFORE, THE PREMISES CONSIDERED, the American Petroleum Institute respectfully urges the Federal Communications Commission to maintain and further the goals of local exchange carrier price cap regulation by taking action consistent with the views expressed herein.

Respectfully submitted,

AMERICAN PETROLEUM INSTITUTE

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18/ *See* Comments of Bell South, pp. 33-39.

CERTIFICATE OF SERVICE

I, Cassandra L. Hall, a secretary in the law firm of Keller and Heckman, hereby certify that a copy of the foregoing was served by hand-delivery on this 29th day of June, 1994, to the following:

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